VZCZCXRO2771
PP RUEHBC RUEHCHI RUEHDBU RUEHDE RUEHDT RUEHFK RUEHHM RUEHKSO RUEHKUK
RUEHLH RUEHNH RUEHPB RUEHPW RUEHROV
DE RUEHKL #1541/01 2910902
ZNY CCCCC ZZH
P 180902Z OCT 07
FM AMEMBASSY KUALA LUMPUR
TO RUEHC/SECSTATE WASHDC PRIORITY 0119
RUEATRS/DEPT OF TREASURY WASHINGTON DC PRIORITY
INFO RUCNASE/ASEAN MEMBER COLLECTIVE
RUEHZU/ASIAN PACIFIC ECONOMIC COOPERATION
RUCNISL/ISLAMIC COLLECTIVE
RUEHGP/AMEMBASSY SINGAPORE 4448
RUEHGV/USMISSION GENEVA 1519

C O N F I D E N T I A L SECTION 01 OF 03 KUALA LUMPUR 001541

SIPDIS

STATE PASS USTR: WEISEL
STATE PASS FEDERAL RESERVE JENNINGS AND O'DAY
STATE PASS FEDERAL RESERVE SAN FRANCISCO TCURRAN
USDOC FOR 4430/MAC/EAP/J. BAKER
TREASURY FOR OASIA AND IRS AND BOUKOL AND CARNES AND
MBEASLEY
STATE PASS OCC NWENTZLER
STATE PASS OTS GAFFIN
GENEVA FOR USTR
SIPDIS

E.O. 12958: DECL: 10/18/2017
TAGS: ECON EFIN EINV MY
SUBJECT: MALAYSIA'S CENTRAL BANK: LET'S MAKE A DEAL!
REGULATION BY NEGOTIATION

Classified By: ECON COUNSELOR MATT J. MATTHEWS, FOR REASONS 1.4 (b) and
(d)

¶1. (C) Summary: A number of U.S. financial services firms operating in Malaysia have described various informal practices undertaken by staff at Bank Negara Malaysia, the Central Bank, designed to encourage US firms to shift investment and jobs to Malaysia in return for regulatory approvals. In some cases the staff's demands to support Malaysian government policies are quite direct, while in other more subtle cases, the central bank,s regulatory and licensing approvals conveniently and predictably follow investment decisions made by U.S. firms that contribute toward the government's development initiatives. U.S. firms attribute these actions by Bank Negara to an effort to earn bragging rights for its support of the GOM,s development plans. Unfortunately, the use of regulatory oversight authority by Bank Negara staff to prod U.S. firms to expand investment and jobs in Malaysia raises serious questions about the central bank's role as a neutral regulator safeguarding financial stability. U.S. firm in Malaysia believe concluding an FTA that includes obligations to liberalize the financial services sector will be the most effective way to address this issue. End Summary.

GETTING CONNECTED REQUIRES "REINVESTING" IN MALAYSIA

¶2. (C) In one case reported to Economic Counselor and Treasury's Financial Attache for Southeast Asia, Bank of America Malaysia (BoAM), a wholly-owned subsidiary of Bank of America (BoA), has been unable to expand its business up to now largely because the central bank, Bank Negara Malaysia (BNM) would not permit the subsidiary to connect to the parent company's Electronic Credit File (ECF), the bank's centralized credit-decision making and risk management tool. Across the globe, BoA approves credit decisions and maintains all its credit files electronically on a single system. In Malaysia, however, BoAM has been forced to make loan applications on paper and send them via fax, maintaining originals in a bulletproof safe.

¶3. (C) In April, after several years of negotiation, BoAM finally secured approval from BNM to connect to its global server by promising to "compensate" for using off-shore credit analysis and risk management tools by "reinvesting" in Malaysia. BNM had cited data secrecy provisions in disallowing the connection, but this prudential issue was not part of the negotiation. Instead, BoAM reported that the key part of the negotiation revolved around the question of what the bank would "bring back into Malaysia" if it were allowed to "take this out."

¶4. (C) Similarly, BoAM has not been able to take advantage of its global internet bank because the server for that was located in Hong Kong. According to one BoAM representative, BNM said connecting to a server outside of Malaysia -- whether for internet banking or credit risk management -- was "outsourcing." When the bank argued that connecting to the box would not result in any Malaysians losing their jobs, BNM countered that, in the event of a financial crisis, foreign banks were likely to "flee the country" unless they had sufficient "brick and mortar" invested here. BoAM responded that, in the event of a disaster, there was no back-up system for its Malaysian customers without a connection to an outside server as is done elsewhere in the region.

¶5. (C) BNM came back to the "brick and mortar" question, pointing out that HSBC had invested $28 million in back-office operations in Cyberjaya, making a significant contribution toward the government's goals of becoming a regional hub for back-office operations and building up the government-initiated cyber-city. BoAM responded that their operations in Malaysia were much smaller than those of HSBC and that $28 million represented roughly half their total business in the country; therefore they could not possibly

commit to such an investment. BoAM asked what was required to "reinvest" in Malaysia, but BNM told them, "We do not have a framework for that." So it became clear, according to the bank representative, that BoAM was expected to bring something to the table. Finally, BoAM offered to build a $1.5 million Global Disaster Recovery Center for its internet banking system and hire two Malaysians to operate the system. BNM then agreed to allow them to connect to the server in the U.S.

DIRECTED LENDING FOR HOUSING AND SMALL BUSINESSES
-- ----

¶6. (C) Directed lending also has been a problem. BNM set an individually-determined housing loan quota for all banks. BNM instructed BoAM to finance 50 low-income housing units (at less than RM60,000 each). BoAM pointed out several difficulties they would have in meeting this quota. First, BoAM did not do private mortgage lending in Malaysia, only corporate lending, and as such would have difficulty in assessing credit risk in this consumer market. Second, very little housing was available at that price in Kuala Lumpur and BoAM had no presence outside the capital city, due to BNM restrictions on foreign conventional banks. Homebuyers from outside the city were unlikely to travel to KL to apply for a mortgage loan, the bank pointed out.

¶7. (C) BNM relented, imposing instead a RM 20 million quota in loans to small and medium-sized enterprises (SMEs). BoAM had been able to meet only about RM 5 million of that quota, so every year it paid a fine. Bank headquarters, however, became increasingly concerned about its reputation risk for not complying with BNM's quota, and sent BoAM back to the negotiating table with BNM. Finally, BNM removed the official quota but established a "target" whereby BoAM was expected to make RM 5.6 million in loans to SMEs, 50% of which must be to SMEs owned by ethnic Malays.

GE COURTS BANK NEGARA

¶8. (C) Separately, Stuart Dean, General Electric President for Southeast Asia, described a similar approach to getting approval from BNM. GE has not been able to enter the Malaysian market because BNM will issue licenses only to banking institutions and GE Money is a finance company. According to Dean, Malaysia has the largest consumer finance market among the five countries in Southeast Asia in which it operates, which also include Thailand, Indonesia, Singapore, and the Philippines. If they could enter the consumer finance market, he argued, GE could double its business in Malaysia.

¶9. (C) Dean described his company's relationship with BNM as "excellent" and said he was optimistic that GE would get the approval they needed. In working with the Malaysian government, it was necessary to show them how Malaysia would benefit from any proposal, he explained. GE recently decided to move 100 of its "backroom" positions to Cyberjaya to serve its clients in Singapore, Hong Kong, and the Philippines. This supports three key goals of the GOM: back-office operations, regional operations, and a boost to the cyber-city. GE also provides scholarships -- another high priority for the GOM which recognizes that the country's acute shortage of skilled labor is one of the major barriers to its development. Last week, press reports announced that GE planned to invest in yet another high-priority government initiative, the "Iskandar Development Region" bordering Singapore, in partnership with the government-linked company UEM World.

SIPDIS

AMERICAN INTERNATIONAL ASSURANCE GROUP

¶10. (C) Brad Bennett, CEO of American International Assurance Group (AIG) said he was confident that the company

would get the approvals it needed because it was contributing to the country's explicit development goals. While the GOM does not state outright that it will award approvals to companies that invest in the government's targeted sectors and initiatives, the company makes the investments and then "trusts" that the regulators will come through. A year ago, Bank Negara was very helpful in working out a solution for AIG's requirements to incorporate locally and meet foreign equity thresholds, and is assisting the company in navigating the approvals required from various ministries for a data/call center to service the region. Bank Negara specifically requested AIG not to publicize its plans to invest in the data/call center. Bennett believes this is to allow Central Bank Governor Zeti to take credit for bringing in this high priority investment. "It will be a political feather in her cap," he told Econoff. AIG's next priority is to get a license for Islamic insurance, as the company perceives that its market share will decline as customers switch from conventional insurance to a Sharia-compliant product.

¶11. (C) Comment: Malaysia has a complex regulatory system whereby approvals are awarded on a case-by-case basis after what often are lengthy negotiations. U.S. companies operating here have spent years investing time and money in the negotiating process and in developing good relationships with Malaysian regulators. U.S. firms do not wish their various ongoing negotiations with Bank Negara to become the subject of government-to-government discussions that could undermine the deals these companies are working so hard to complete. However, these financial sector companies do hope that the successful conclusion of an FTA with Malaysia will create a more transparent and liberalized operating environment which will eliminate the need for such

interactions with Bank Negara in the future. Finally, the aggressive effort by Bank Negara to use what should be prudential or regulatory tools for the benefit of unrelated government policies should raise some questions about how it will implement any "prudential carve outs" in the FTA. Clearly some of the policies imposed by BNM on the banks actually undermined their global risk management capabilities. End Comment.

KEITH